



January 2, 2001

Office of Policy
Office of Economic, Electricity and Natural Gas Analysis PL-21
Attn: Electric Reliability Comments
U.S. Dept. of Energy
Forrestal Building, Room 7H-034
1000 Independence Avenue, S.W.
Washington, DC 20585

Re: Electric Reliability Issues – Notice of Inquiry

Dear Madam/Sir:

These comments are submitted on behalf of Colorado Springs Utilities (CSU). CSU is an enterprise of the City of Colorado Springs, Colorado. CSU operates as a vertically integrated electric utility providing service to approximately 175,000 retail customers within the City of Colorado Springs and adjoining areas of El Paso County, Colorado. CSU also provides wholesale power to the City of Fountain, Colorado, also located within El Paso County.

CSU owns and operates approximately 620 megawatts of electric generation capacity, including coal-fired, gas-fired, and hydropower units, all of which are located within El Paso County. In order to deliver power to load, CSU also operates approximately 206 miles of high voltage transmission infrastructure within El Paso County. The peak load for CSU recently reached 743 megawatts. To meet this load, the CSU generation is supplemented by contract purchases from the Western Area Power Administration and Enron Power Marketing, Inc.

CSU is active in national and regional reliability organizations. CSU is a member of the North American Electric Reliability Council (NERC) and is represented on the NERC Interchange Subcommittee and until recently on the NERC Performance Subcommittee. CSU is also a member of the Western Systems Coordinating Council and the Rocky Mountain Reserve Group. CSU has adopted an open access transmission tariff and standards of conduct pursuant to Orders 888 and 889 and has received non-jurisdictional rulings from the FERC as to both its tariff and standards of conduct. Currently, CSU is actively involved in the efforts to create a regional transmission organization denominated "DesertSTAR".

CSU appreciates this opportunity to comment concerning the possible creation of a mandatory reliability structure through a subsequent rule-making. Although CSU will comment on only certain of the specific issues raised in the November 20, 2000 Notice of Inquiry, it wishes to first address two threshold issues: the first being the premise that the electric industry is moving rapidly toward retail competition; and, the second involving the pace and direction of restructuring and the potential for unintended consequences associated with this rule-making.

Threshold Issues

The inevitability of retail competition is an assumption which seems to underlie the NOI. For example, the NOI quotes from the 1998 Final Report of the Secretary of Energy Advisory Board's Task Force on Electric System Reliability to the effect that:

The energy industry is in a transition from a highly regulated industry dominated by monopoly utilities to an industry that will rely, in large part, upon competitive commercial markets at both the wholesale and retail levels.

CSU suggests that the rush for state implementation of retail competition may not be as inevitable as it appeared to be during 1998. Many states -- including Colorado -- have firmly rejected efforts to introduce competition at the retail level. The potential effects of retail competition were the subject of an extensive eighteen (18) month study funded by the Colorado General Assembly and conducted by an appointed Electricity Advisory Panel. After months of extensive study the majority of the Panel concluded that retail competition would not be in the best interests of all Colorado consumers. Recent events in California have further called into question the wisdom of retail restructuring unless and until there is a balance between supply and demand sufficient to produce a workable power market; a situation which presently does not exist in Colorado and much of the Western United States.

Certain states may continue to experiment with direct retail competition where local circumstances accommodate a competitive environment. This is entirely appropriate. However, for a great number of states, retail competition will not occur within the near future because in many areas of the country the risk is too great that direct retail competition will not offer benefits to consumers. This concern is particularly acute in states with electric rates below the national average; again, Colorado and many other Western States fall into this category. Consequently, CSU urges the Department of Energy and the FERC to closely examine the reasonableness of the assumptions concerning a speedy, nationwide conversion to direct retail competition. Under no circumstances should regulatory standards be adopted under the guise of enhancing reliability which have the intent or effect of fostering retail competition.

The need to closely examine assumptions regarding the market penetration of direct retail competition leads into the second threshold issue, that being the rapid pace of industry restructuring and the potential for unintended consequences that result from “top down” regulatory changes. Until recently, the electric industry in the United States had functioned for over one hundred years as a highly regulated industry composed of monopolies offering exclusive utility service within defined areas. It has been only within the last ten years that this organizational model has come under significant challenge. Much of the modification to the traditional industry model have occurred at the federal level in the context of wholesale power sales and transmission service. Largely under the auspices of the FERC, the bulk transmission system has been converted to open access allowing a greater degree of competition for wholesale power supplies. The FERC has recently taken another step toward creating what amount to regional freetrade zones through the adoption of Order 2000.

CSU views these as positive developments, but is concerned that the pace of restructuring may be moving so quickly that markets and business practices are not given the opportunity to evolve in a manner which recognize benefits for market participants. CSU is firmly convinced that open transmission access and a workable wholesale power market will benefit utilities and consumers once they have been fully developed; however the recent experiences of CSU operating under the unbundled system have involved higher costs and an increased level of frustration with the complexity of routine transactions. For example, the open access transmission tariffs as filed under the FERC-approved methodology have led to transmission pricing increases of approximately 30% in this region. The price of wholesale power within this region has also recently increased greatly, with the annual average cost being higher by a factor of three. The complication of routine transactions has also increased under the open access format. Transactions are now often segmented so that what was at one time a single transaction, is now often three or four separately scheduled transactions. This not only increases the costs of transactions, but also places a burden on operating personnel who often feel overwhelmed with the increasing complexity.

The point of this discussion is that reforms intended to increase market efficiency have, in the short-term, often resulted in inefficiencies. These problems are not insurmountable, but the pace of restructuring should be tempered to allow an adequate opportunity to address short-term inefficiencies. Accordingly, CSU urges a cautious and incremental approach, wrinkles should be ironed out and benefits enjoyed prior to a new wave of restructuring activity. In adopting national reliability standards, the Department of Energy and the FERC should first determine whether or not true reliability issues exist or whether reliability problems are a reflection of market conditions which may be corrected through a “settled” wholesale power market fully adapted to the changes which have been effected by Orders 888 and 889.

Regarding the specific issues for which the Department of Energy requests comment, CSU states as follows:

1. *Is the existing arrangement of voluntary compliance with industry reliability rules sufficient to ensure reliability of the bulk power transmission system?*

Response: CSU believes the existing arrangement of voluntary compliance with industry standards has functioned remarkably well during the past 35 years. Despite CSU's belief that retail competition may not become the industry norm within the near future, there has been a significant increase in competition within the wholesale power market. Increased wholesale competition has resulted in a number of new market participants which do not fit within the traditional and homogeneous industry mold of vertically integrated monopolies.

New market players with differing business interests and perspectives on reliability may create stresses within the existing voluntary arrangement; however, it may be too soon to conclude that the present system will become unworkable. Conversely, it is possible that the recent advent of a true wholesale market has created a number of short-term dislocations which may have no long-term adverse affect on reliability. Accordingly, CSU favors a systematic review of reliability in the context of recent market reforms in order to identify the presence and nature of reliability threats prior to any comprehensive rule-making.

3. *If FERC has the authority to establish and enforce reliability standards, may FERC delegate such authority to a self-regulating reliability organization? Should it do so?*

Response: CSU takes no position on the legal issue of the ability of the FERC to delegate rule-making authority to a non-governmental organization. Assuming that FERC has the legal authority to delegate such rule-making functions, CSU supports the creation of national standards, if -- and only if -- reliability issues are truly present. Consistent national reliability standards, which extend no further than necessary to address specifically identified problems, fit neatly with the consistency FERC has created through Orders 888, 889, and 2000. But if national rules are to be promulgated, CSU favors a cautious and light-handed regulatory approach which recognizes and accommodates regional differences. As will be discussed further below, CSU believes that generalized national standards offering sufficient latitude to meet regional differences are preferable to a series of regional substandards which may segregate the wholesale power market.

If a rule-making is pursued to effect delegation of regulatory standards to a national reliability organization, the FERC should establish sufficient due process protections in order that all relevant and affected players can participate in the process during which such standards are adopted. Moreover, any delegation should mandate the establishment of threshold cost/benefit analyses

supporting any standard eventually adopted. Reliability is an important feature of the electric industry, but the FERC and its delegee must be cognizant that all regulatory actions encounter a point of diminishing returns. The standards should seek to maximize reliability at a reasonable cost to market participants.

The proposed Comprehensive Electricity Competition Act contained provisions for the sub-delegation of rule-making authority to regional reliability organizations. CSU is concerned that sub-delegation could jeopardize the consistency that the FERC is fostering in other areas of electric restructuring. In essence, sub-delegation could lead to a Balkanization of the wholesale power market through the creation of regional reliability standards which impede market development. If the FERC is inclined to allow sub-delegation, two safeguards should be put in place: (1) a more stringent standard must be provided for the adoption of regional standards, and (2) prior to becoming effective, any regional standard must be submitted for review by the national reliability organization, with that organization having final affirmation authority over regional action.

CSU appreciates the opportunity to file these comments.

Sincerely,

Mirek Horenovsky
Division Manager